
NEW PERSPECTIVES ON CONNECTICUT'S CHANGING ECONOMIC LANDSCAPE

entrepreneurial efficient dynamic versatile responsive trusted creative progressive visionary

Presented by:

***The Governor's Council
of Economic Advisors***

November 12, 2009

GOVERNOR'S COUNCIL OF ECONOMIC ADVISORS

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-) **Nick Perna, Ph.D., Perna Associates, Yale University Economics Dept.**
-) **John Tirinzonie, State Labor Economist, Connecticut Department of Labor**

DON KLEPPER-SMITH:

-) Chief Economist, DataCore Partners LLC**

TOPICS:

-) 3Q REAL GDP TURNS POSITIVE**
-) U.S. AND CT. JOB GROWTH EXPECTED TO LAG**
-) OVERALL GROWTH IN CT: TD BANK BUSINESS BAROMETER**
-) SUMMARY: KEY POINTS**

3Q09 REAL GDP DATA MARKS AN END TO THE RECESSION!

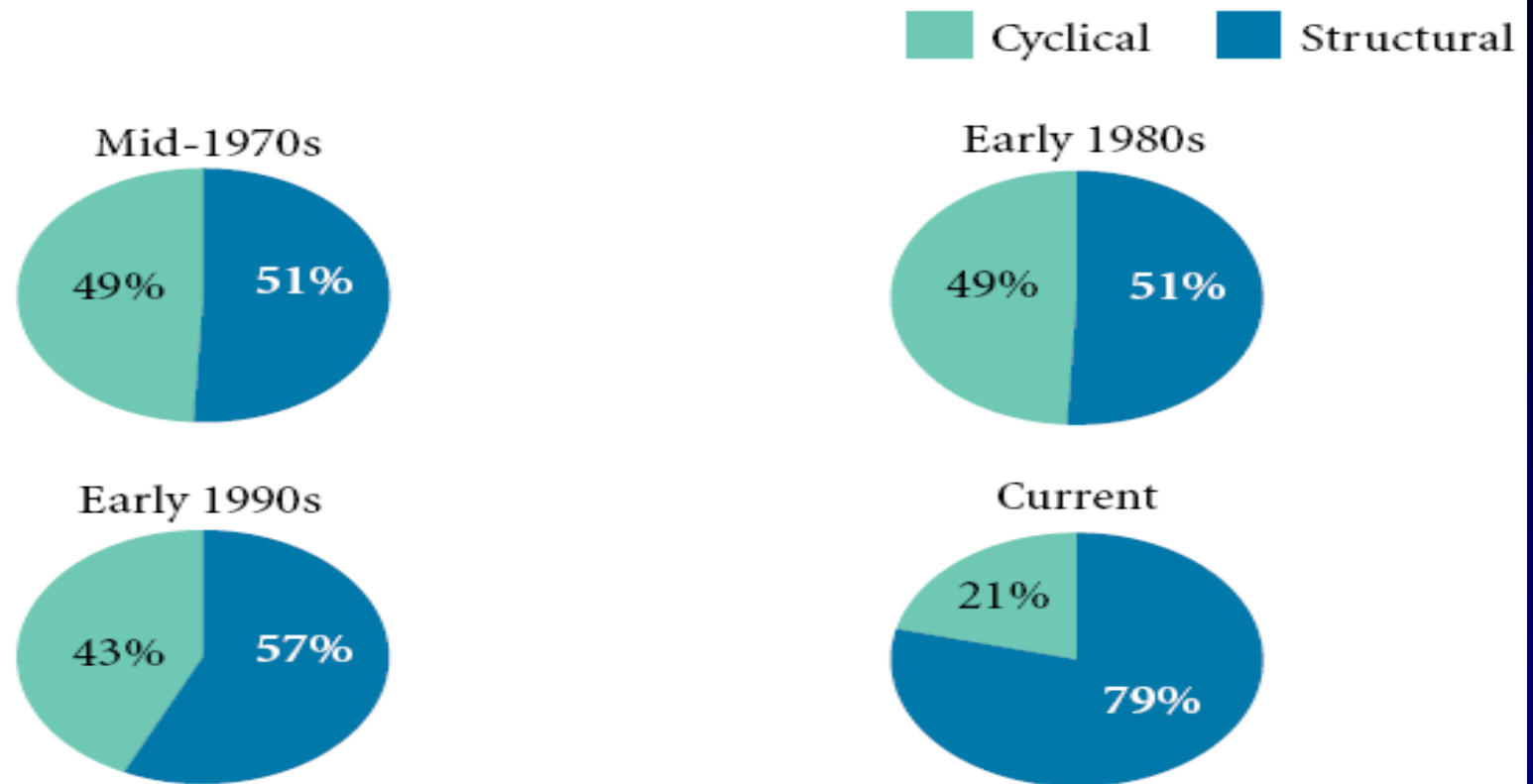
-) THE U.S RECESSION ENDED IN 3Q09 AS REAL GDP ROSE AT A SAAR OF 3.5%. MONETARY AGGREGATES HAVE BEEN RAPIDLY INCREASING AND U.S. FISCAL POLICY HAS BEEN HIGHLY STIMULATIVE.**
-) HOWEVER, THIS “END OF RECESSION” CALL IS APT TO SEND MIXED MESSAGES AND WILL CONFUSE MANY AS BOTH U.S. AND CT. LABOR MARKETS ARE NOT EXPECTED TO BOTTOM UNTIL MID-2010.**
-) WHEN ASKING THE KEY QUESTION AS TO WHAT CONSTITUTES “ECONOMIC RECOVERY”, MOST WOULD ARGUE THAT ECONOMIC EXPANSION WITHOUT TANGIBLE JOB GROWTH IS NO RECOVERY AT ALL. THEREFORE, A “JOBLESS RECOVERY” IS THE MOST LIKELY SCENARIO TO UNFOLD IN COMING QUARTERS.**

JOB GROWTH IS LIKELY TO LAG

-) IN THE NEXT UPCYCLE, JOB GROWTH IS LIKELY TO BE A LAGGING ECONOMIC INDICATOR AS EMPLOYERS ARE NOT APT TO ADD TO THEIR EXISTING WORKFORCE UNTIL BUSINESS ACTIVITY REALLY BOOMS.
-) ON THE FRONT END OF THE BUSINESS CYCLE, IT'S ALL ABOUT PRODUCTIVITY GROWTH - DOING MORE WITH LESS!
-) LOOK FOR A RISE IN WORKWEEK HOURS ON THE FRONT END OF EXPANSION: PRIVATE SECTOR WORKWEEK AS OF 10/09: 33.0!
-) MOREOVER, PRODUCTIVITY IS A FUNCTION OF EITHER CAPITAL OR LABOR. TODAY, GIVEN THE LOW INTEREST RATE ENVIRONMENT, MANY FIRMS MAY CHOOSE TO SUBSTITUTE CAPITAL FOR LABOR, SUBDUING FUTURE JOB GAINS.
-) MOST IMPORTANTLY, PROFOUND STRUCTURAL CHANGE- CHANGE APART FROM THE NORMAL BUSINESS CYCLE- IS BECOMING MORE APPARENT IN THE DOMESTIC LABOR MARKETS. IN THE NEW WORLD ECONOMIC ORDER, JOBS ARE INCREASINGLY TRANSPORTABLE AND WILL MIGRATE TO LOW COST REGIONS IN ORDER TO BOOST CORPORATE PROFITS AND BUSINESS PRODUCTIVITY.

U.S. JOB LOSSES ARE INCREASINGLY STRUCTURAL, NOT CYCLICAL

Share of Total Employment in Industries Undergoing Cyclical Changes and in Industries Undergoing Structural Changes



Sources: U.S. Bureau of Labor Statistics; authors' calculations.

SOURCE: NY FED AUG 2003 REPORT. STRUCTURAL CHANGE INVOLVES LT COSTS OF DOING BUSINESS, FACTORS INVOLVING GLOBALIZATION, SUBSTITUTION EFFECT, DOWNSIZINGS, AND OTHER NON-BUSINESS CYCLE FACTORS.

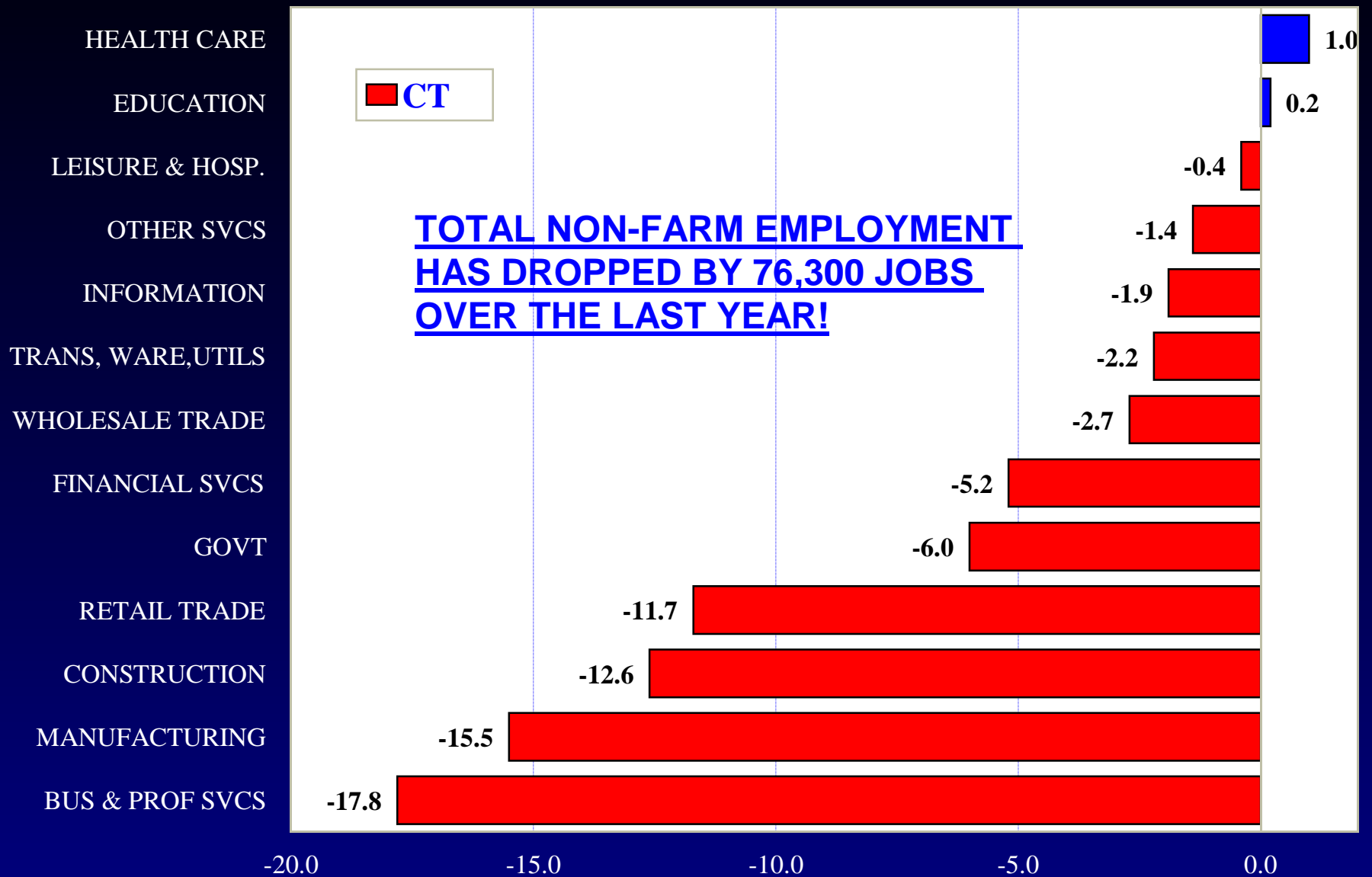
CONNECTICUT AVERAGE ANNUAL TOTAL NON-FARM EMPLOYMENT LEVELS, (THOUSANDS, 1980-2010)



Source: Ct Labor Dept.

2009-2010 Projections from DataCore Partners LLC

ABSOLUTE CHANGE IN CT. EMPLOYMENT (000) BY SECTOR, SEPT 08- SEPT 09



TD BANK **BUSINESS BAROMETER** **(TDBBB)**

**COINCIDENT INDICATOR OF ECONOMIC ACTIVITY
WITHIN CONNECTICUT**

FORMED FROM THREE STATEWIDE SERIES:

- MANUFACTURING PRODUCTION**
- NON-MANUFACTURING EMPLOYMENT**
- REAL DISPOSABLE INCOME**

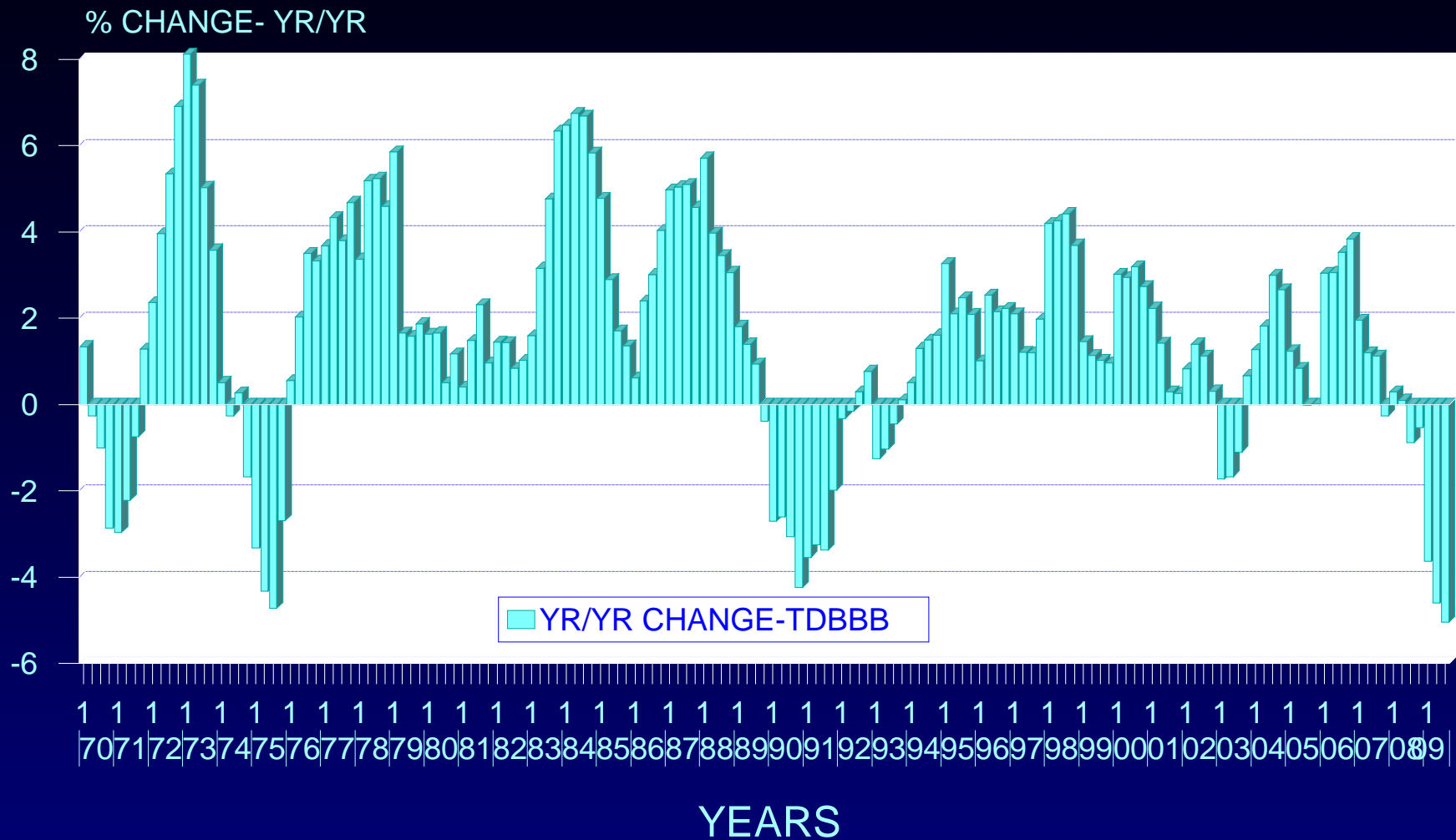
**RELIABLE BAROMETER WITH RESPECT TO THE
MAGNITUDE AND DIRECTION OF OVERALL
ECONOMIC EXPANSION**

TD BANK BUSINESS

BAROMETER REVISIONS (10/09)

-) **OVERVIEW:** NEW DOL ESTIMATES OF NOMINAL PERSONAL INCOME, WHICH REPRESENTS OUR COLLECTIVE EARNING POWER, REFLECT AN ECONOMY THAT IS CONSIDERABLY WEAKER THAN ORIGINALLY THOUGHT. NOMINAL INCOME IS NOW EXPECTED TO FALL MORE THAN 4% IN 2009.
-) **ACTUAL DATA THROUGH 3Q09 SHOWS THE TDBBB FALLING 5.0% IN 3Q09 ON A YR/YR BASIS, NOW DOWN 4.4% CUMULATIVE YTD.**
-) TDBBB IS NOW EXPECTED TO FALL BY 4.0% IN 2009 AND CLIMB JUST FRACTIONALLY IN 2010.

TD BANK BUSINESS BAROMETER (YEAR OVER YEAR % CHANGE) (70Q1-3Q09)

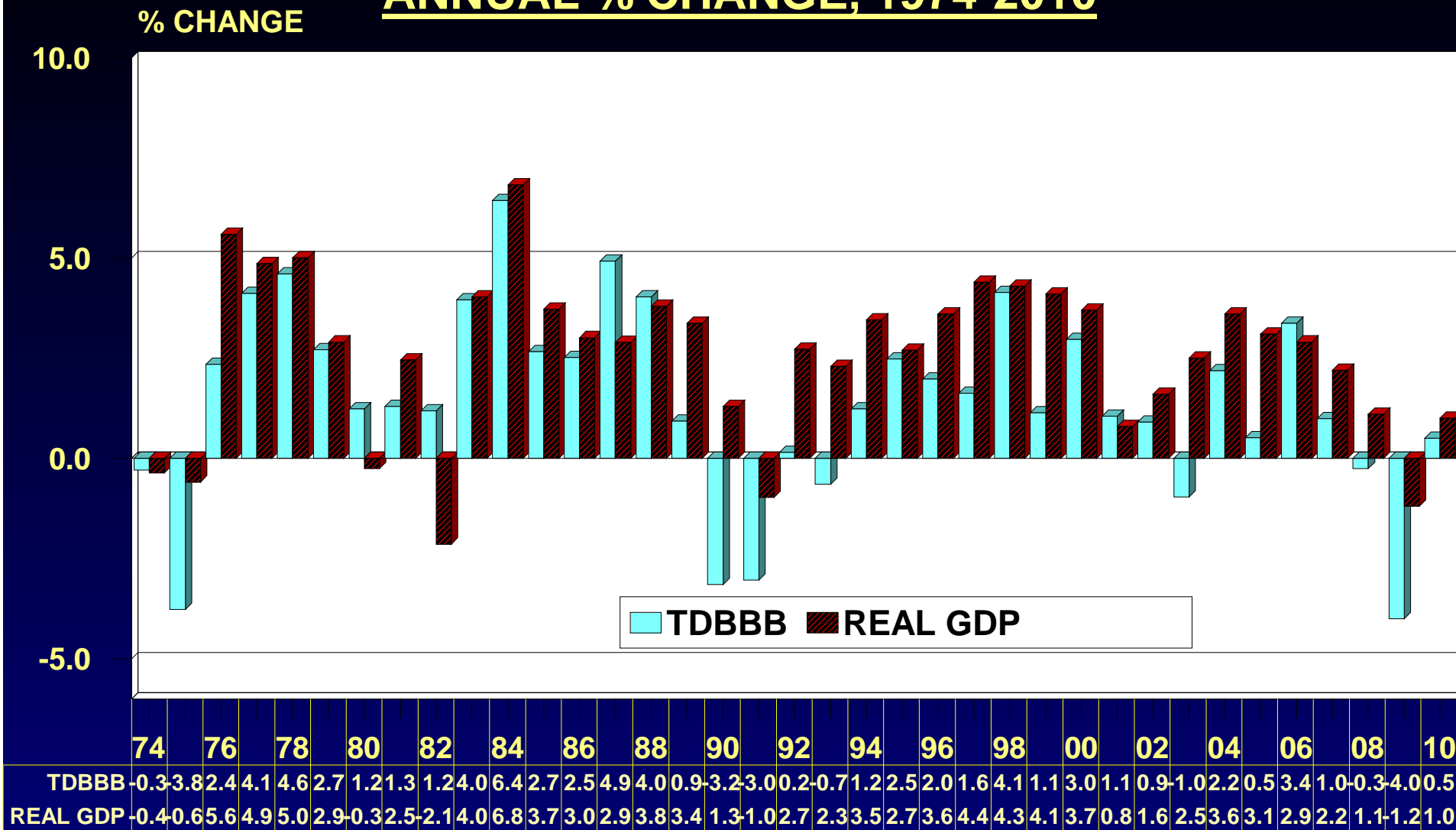


NOTE: REFLECTS 3/09 LABOR DEPT REVISIONS

U.S. VS CONNECTICUT BUSINESS CYCLES

REAL GDP VS. TD BANK BUSINESS BAROMETER

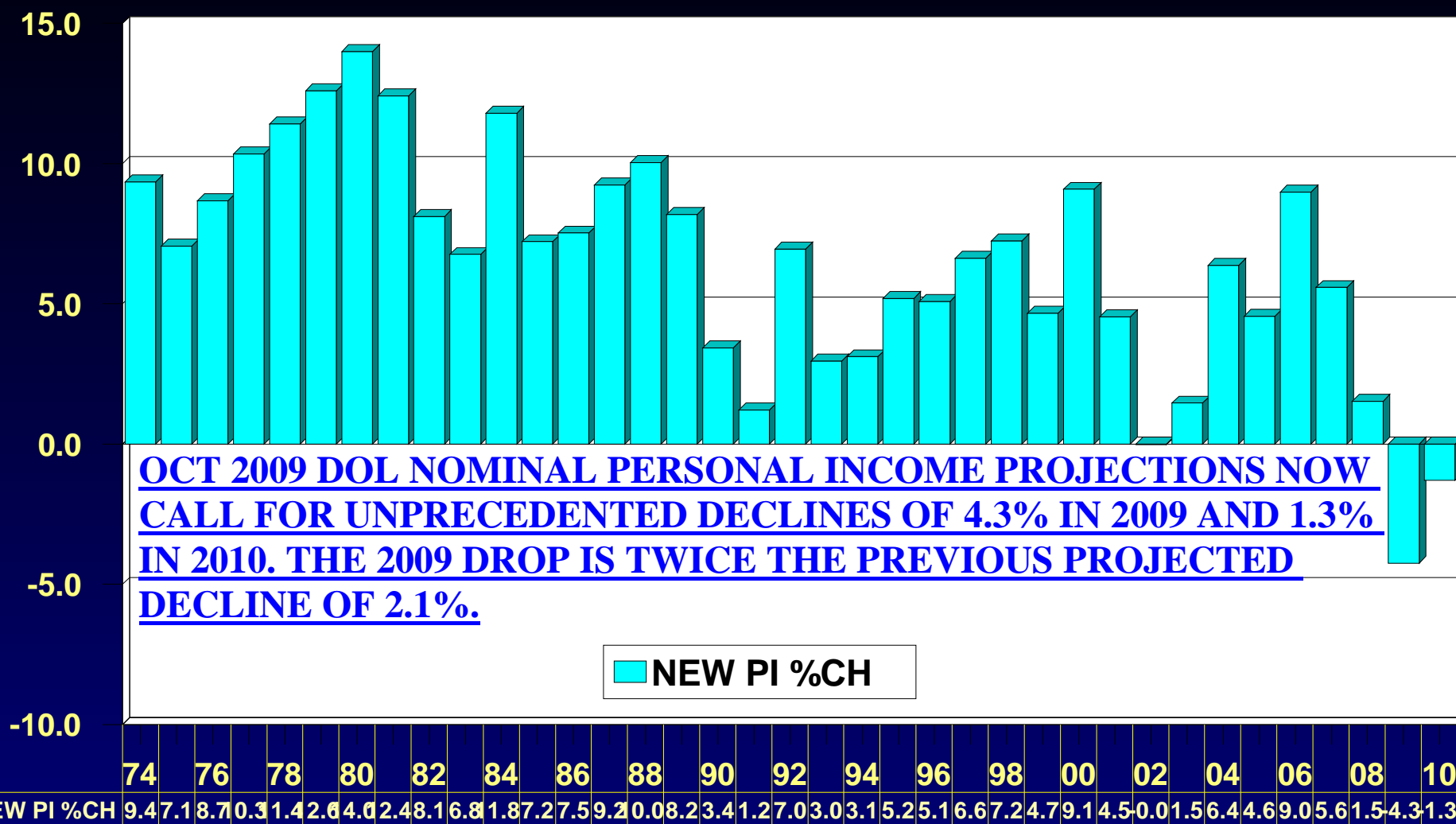
ANNUAL % CHANGE, 1974-2010



Source: DataCore Partners LLC, U.S. Commerce Dept.,
 Note: Reflects 10/09 Data Revisions; Forecast Begins 2009

CONNECTICUT NOMINAL PERSONAL INCOME ANNUAL % CHANGE, 1974-2010

% CHANGE NEW PI SERIES AS OF OCTOBER 2009



Source: U.S. Commerce Dept.,

Note: Reflects 10/09 Data Revisions; DOL Forecast Begins 2009

CT. ECONOMIC SUMMARY

-) THE CT. ECONOMY IS STILL FACING HEADWINDS FROM THE NATIONAL RECESSION. TD BANK BUSINESS BAROMETER: 2009: -4.0%, 2010:+0.8%
-) LOCAL LABOR MARKETS ARE EXPECTED TO WEAKEN INTO 2010, WITH PEAK TO TROUGH JOB LOSSES FOR CT. AT ROUGHLY 100,000. RISKS TO THE FORECAST CATEGORICALLY LIE TO THE DOWNSIDE, MEANING HIGHER JOB LOSSES, NOT FEWER. JOBS WILL LAG ON THE FRONT END OF THE BUSINESS CYCLE. CURRENT JOB LOSS: 86,800.
-) BOTTOM LINE: CT INCOME TAX AND SALES AND USE TAX REVENUES ARE EXPECTED TO REMAIN WEAK OVER THE NEAR-TERM.
-) - NEW ENGLAND CONSUMER CONFIDENCE IS DOWN 19% YTD (10/09)
-) - LABOR MARKETS EXPECTED TO SOFTEN OVER THE NEXT 2-3 QUARTERS.
-) - CT NOMINAL PERSONAL INCOME IS POISED TO DROP 4.3% IN 2009.
-) - “WEALTH EFFECTS” FROM HOUSING & STOCKS DAMPENS CONSUMPTION.
-) - CONSUMERS ARE NOW REPLENISHING SAVINGS & SPENDING LESS.

NICK PERNA:

-) Ph.D., Perna Associates, Yale University Economics Dept.**

RECESSION IS OVER

Ended: August or September 2009

Started: December 2007

At 20-21 months, almost double post
WWII average

Terminology:

Recession over: GDP stops declining

Recovering: getting better

Recovered: back to pre-recession level

CURRENT STATUS

- GDP: recovering ... below '07
- Stocks: recovering ... 27% below '07
- House prices: recovering ... 33% below '06
- Unemployment: still deteriorating ... more than double pre-recession 2007 level (10.2% vs 4.4%)
- Jobs: still declining ... 7.3 million below '07

WHAT'S NEXT: U,V,W,L?

U.S. Economic Forecast *Wall Street Journal Survey (Oct. 2009)*

	2009 Q1	Q2	Q3	Q4	2010 Q1	Q2	Q3	Q4
REAL GDP % CH	-6.4	-0.7	3.5	2.5	2.6	2.8	2.9	2.9
CPI % CH		0.7		1.6		1.8		1.8
UNEMPLOYMENT %		9.5		10.0		9.9		9.4
FED FUNDS %		0.13		0.16		0.38		0.97
10-YR TREASURY %		3.52		3.58		3.90		4.24

GDP percent change is from previous quarter at annual rate. CPI is end of quarter month from 12 months earlier.
Unemployment and interest rates are June and December levels

HOW LONG TO *RECOVER*?"

Unemployment down to 5% 5-6 years

House prices back to 2006 5-6 years

Dow Jones again above 14,000 ???

after 1929: took 25 years

after 1973: took 10 years

Rapid return to "normal" highly unlikely

MUCH DOWNSIDE RISK

- **Consumer confidence slips**
- **Foreclosures rise further**
- **Financial institutions falter**
- **Stock market plunges**
- **\$ exchange rate plunges**
- **Inflation surges**

SUSAN COLEMAN:

-) D.P.S., Professor of Finance,
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Labor Markets:

- Although the pace of job losses has slowed, employers are still not adding jobs yet.
- Rather, they are relying on productivity improvements (9.5% annualized in 3rd Q); doing more with less.
- Will expand workweek and use overtime and temps before hiring.
- Average workweek is only 33 hours, so there is still considerable slack in the system before employers need to hire.

Consumer Spending:

- Many consumers do not have either the means or the will to spend.
- Drags on consumer spending:
 - High level of unemployment (10.2%)
 - Job losses will extend into 2010
 - Wage income is more than 5% below year ago levels
 - Negative wealth effect despite recent stock market gains
 - Restrictive consumer lending standards
 - End of Cash for Clunkers

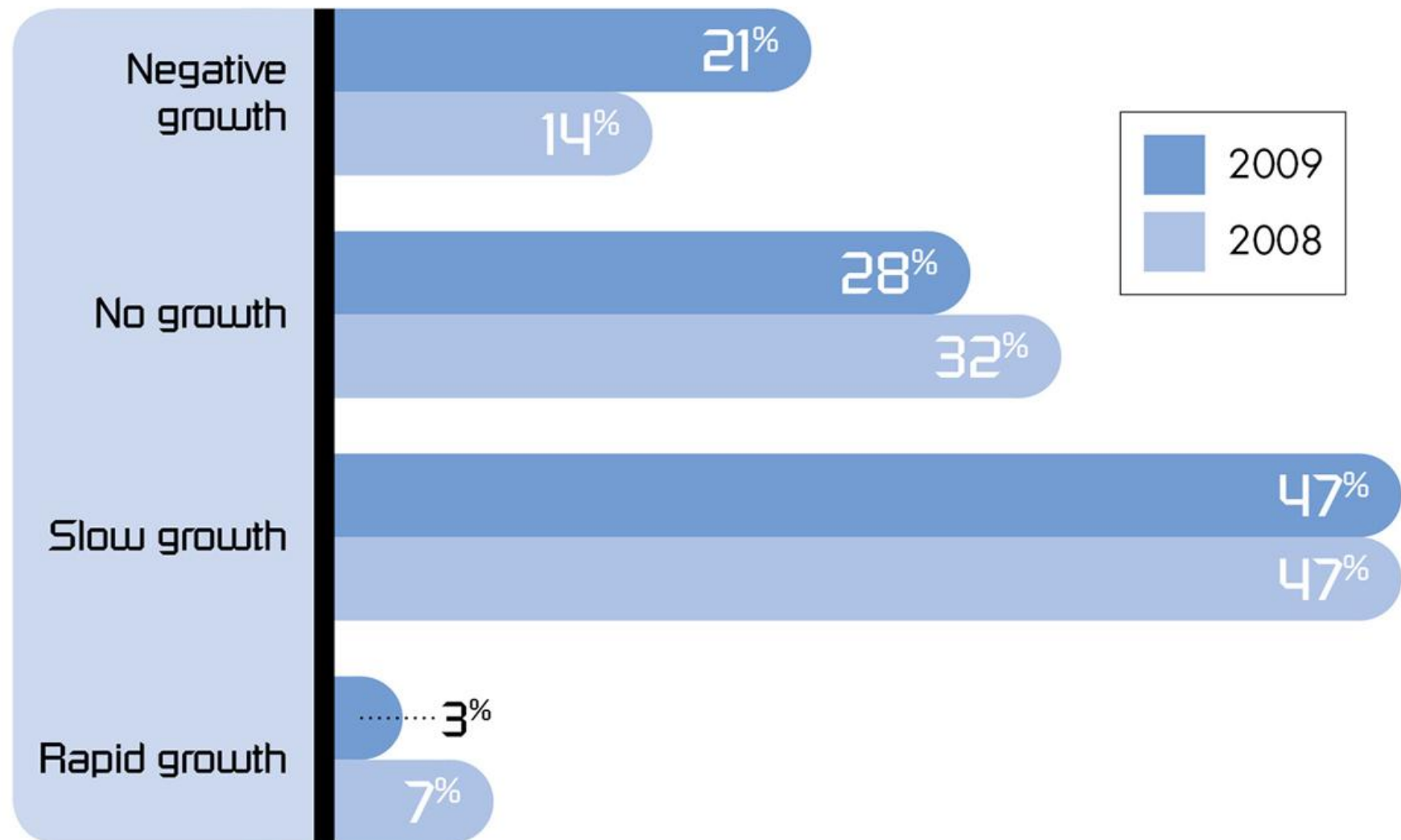
Consumer Confidence

- Has rallied somewhat, but remains depressed.
- Concerns:
 - Fragile job market
 - Decline in home values
 - Battered 401k's and stocks
 - Rising oil and gas prices
 - Uncertainty about health care legislation and how it will affect them
 - Size of federal and state budget deficits and future tax levels

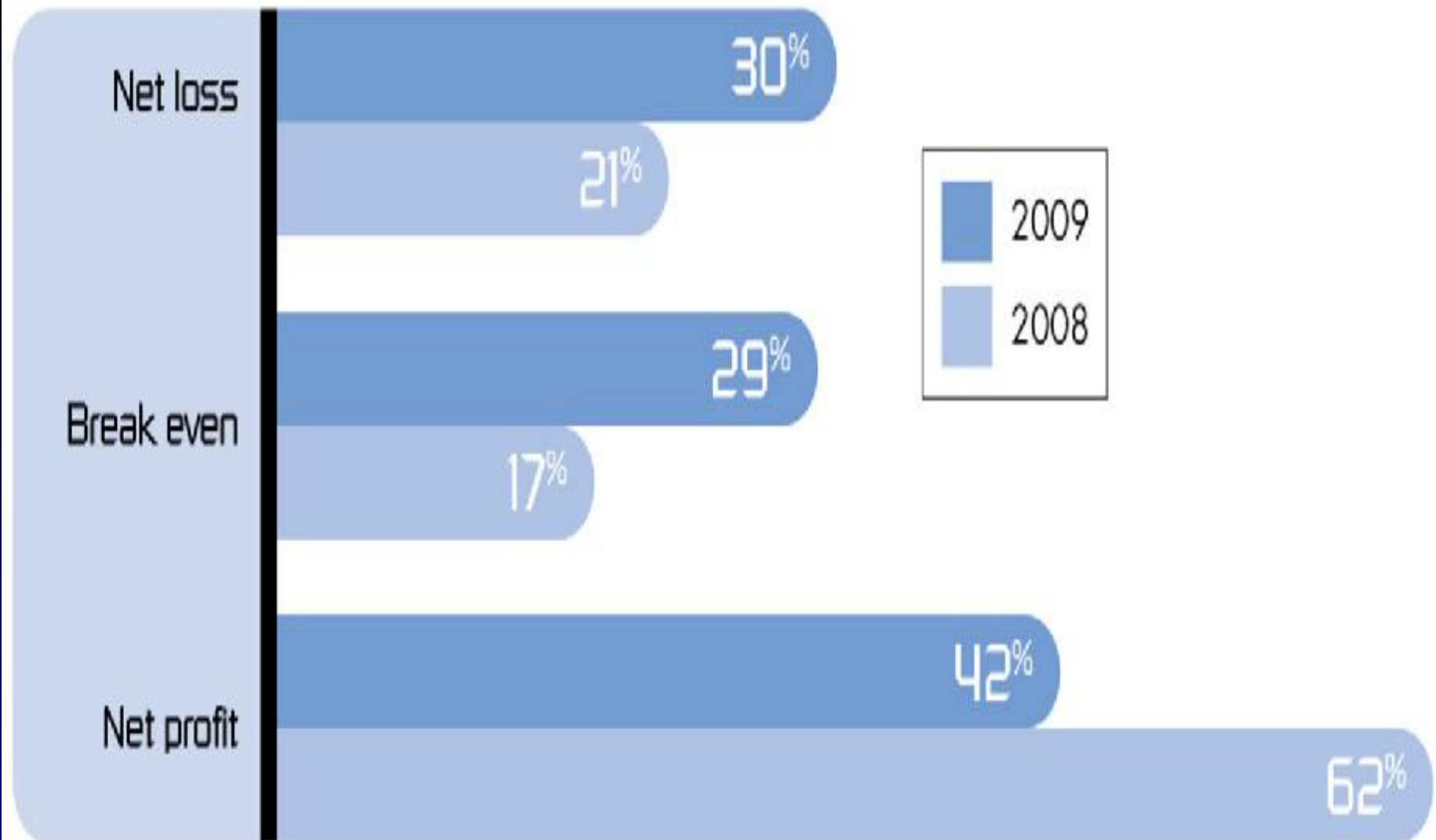
PETE GIOIA:

-) VP & Chief Economist, Connecticut Business & Industry Assn.**

Anticipated business growth, next 12 months



Business profitability, 2008–2009



CBIA MEMBERSHIP SURVEY
Q: CURRENT OUTLOOK FOR FIRM?

	<u>3q08</u>	<u>4q08</u>	<u>1q09</u>	<u>2q09</u>	<u>3q09</u>
Improve	22%	12%	20%	18%	27%
Remain Stable	41%	37%	38%	49%	44%
Worsen	37%	50%	42%	33%	29%

CBIA MEMBERSHIP SURVEY
Q: OUTLOOK FOR PRODUCTION/SALES?

	<u>3q08</u>	<u>4q08</u>	<u>1q09</u>	<u>2q09</u>	<u>3q09</u>
Improve	30%	17%	24%	25%	28%
Remain Stable	36%	30%	34%	39%	37%
Worsen	35%	54%	42%	37%	35%

CBIA MEMBERSHIP SURVEY
Q: PRODUCTIVITY OUTLOOK?

	<u>3q08</u>	<u>4q08</u>	<u>1q09</u>	<u>2q09</u>	<u>3q09</u>
Improve	35%	22%	30%	24%	35%
Remain Stable	48%	48%	46%	55%	47%
Worsen	18%	30%	24%	21%	19%

CBIA MEMBERSHIP SURVEY

Q: OUTLOOK FOR SIZE OF FIRM'S WORKFORCE?

	<u>3q08</u>	<u>4q08</u>	<u>1q09</u>	<u>2q09</u>	<u>3q09</u>
Improve	15%	10%	14%	10%	7%
Remain Stable	61%	52%	52%	58%	64%
Worsen	24%	38%	35%	32%	29%

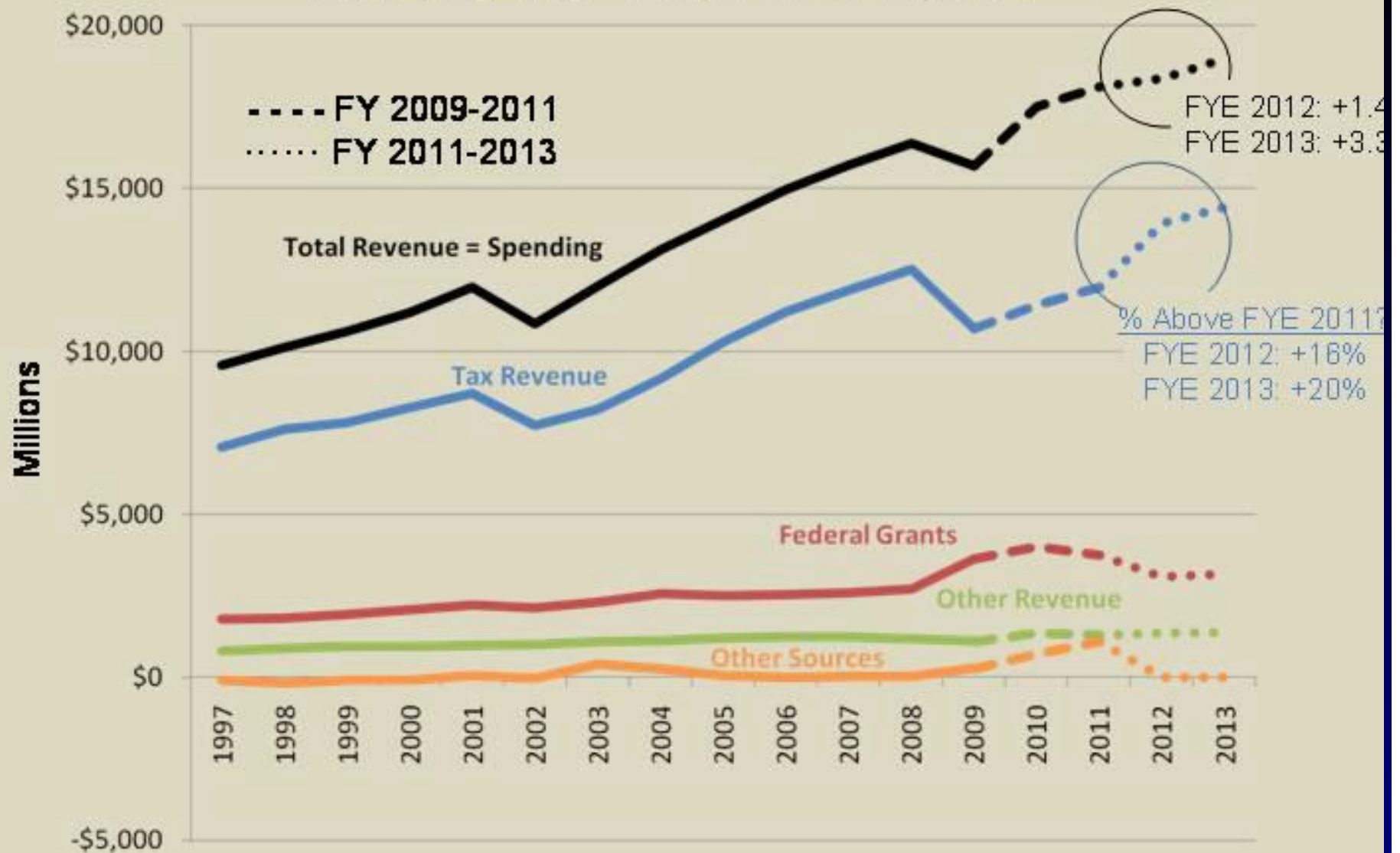
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GROWTH IN STATE TAX REVENUE AVERAGES 5%, WITH CONSIDERABLE VOLATILITY



ACCOUNTING FOR STATE REVENUE, PAST, PRESENT AND FUTURE



5% TAX REVENUE GROWTH OPENS UP BILLION-DOLLAR BUDGET GAPS



MORE BAD NEWS

- Current budget already in deficit, so add any current shortfalls to the anticipated gaps
- Analysis doesn't include unfunded pension and other post employment benefit liabilities that exceed the size of the general fund
- Makes no allowance for a rainy-day set-aside or retirement of deficit bonds
- Current debt levels--8.2% of personal income v. 2.5% nationally--third-highest in U.S.
- Below-average income growth means 5% revenue growth assumption could be unrealistic